AMERICAN FOREIGN POLICY COUNCIL

What Iran Gets from the Strategic Deal with China

July 29, 2020 *The Navigator*

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A new day is dawning in Sino-Iranian relations. Earlier this month, Iranian officials revealed publicly that they were in the final stages of negotiations with China on a sprawling, 25-year strategic pact. The deal will, if implemented in full, dramatically expand military, economic, and political ties between the two countries. The new accord should not be surprising; Tehran and Beijing have historically cooperated on everything from arms sales to energy. Even so, the agreement – which is scheduled to be finalized in coming weeks – represents a landmark expansion of bilateral relations between the two strategic partners. It is also a development with major implications for regional geopolitics and a clear threat to the United States' efforts to isolate and contain the Islamic Republic.

A Lifeline for Tehran

For Iran, the decision to deepen strategic ties to China reflects the recognition that, after almost two years of the Trump administration's "maximum pressure" policy, the country's clerical regime is far weaker than commonly understood. To be sure, Iranian officials have attempted to put on a brave face regarding their geopolitical and economic situation. In July, for example, Iranian Vice President Eshaq Jahangiri asserted publicly that, in spite of U.S. sanctions, the Iranian economy is "back on its feet and growing."

The numbers, however, tell a very different story. Over the past year, the country's oil revenues declined by some 92%, from around $100 billion to just $8 billion. This declining income reflects a massive cooling of Iran's oil sector, as skittish clients fearful of the potential consequences from the U.S. sanctions on Iran increasingly disengage from the Islamic Republic. Indeed, Iranian officials recently disclosed that a growing number of the regime's foreign partners are declining to sign new energy deals with Tehran.

Foreign investment in Iran has dried up as well, as more and more countries and businesses have opted to steer clear of the Islamic Republic rather than risk becoming the target of U.S. sanctions. According to the U.N. Conference on Trade and Development, foreign direct investment in Iran declined by 26.5 percent in 2019 and now stands at its lowest level in nearly two decades.

These factors have precipitated a full-on collapse of Iran's national currency. This summer, the Iranian rial – which traded at 79 to the U.S. dollar at the time of the 1979 Revolution – plummeted to its lowest rate in the Islamic Republic's 41-year history (260,000 to $1). So steep was this decline that the country's Central Bank spent close to $1 billion in recent days to stabilize the failing currency.

Thus, the Iranian regime has been forced to eat into its savings in order to stay afloat. Even prior to the coronavirus, the prestigious Institute for International Finance was estimating that Iran's foreign exchange reserves – which held more than $100 billion in 2019 – would dip to some $73 billion in the first half of this year, and at the current rate of consumption total just $20 billion by March 2023. With the outbreak of the global pandemic, that trajectory has become steeper still, as Iran's regime has been forced to further deplete already-scant funds to address the nation's health crisis.

In turn, Iran's deteriorating internal conditions have bred growing domestic unrest. The persistent grassroots dissent of the past two years – temporarily quelled as a result of the coronavirus – has re-emerged in recent weeks. Sporadic anti-regime demonstrations in various cities over issues such as the country's currency crisis, regime mismanagement of the pandemic, and rising unemployment have given Iran's leaders an additional challenge to regime stability.

These harsh realities appear to have forced a strategic rethink in Tehran. Iran's leaders had originally opted for a policy of "strategic patience" in response to mounting U.S. pressure, hoping simply to hang onto power until a friendlier administration (one more amenable to compromise with Iran's leaders) came to power in Washington. But amid increasingly adverse domestic conditions, Iran's leaders appear to have concluded that their situation is untenable and urgent. Their tilt toward China reflects a recognition that they require external assistance to stay solvent and improve their international position – even if Beijing's aid is accompanied by what amounts to a significant erosion of national sovereignty.

Consequences of the Compact

How will Chinese assistance aid the Iranian regime? For now, the particulars are impossible to discern. Yet at least two broad strategic outcomes are likely to flow from the new Sino-Iranian pact.

The first has to do with Iran's regional posture. Over the past two years, escalating U.S. sanctions have begun to significantly impact the Islamic Republic's strategic standing, as well as its ability to shape regional events. Dwindling financial support to Lebanon's Hezbollah and a loosening of Iranian control over Iraq's powerful Shiite militias are just some of the developments that can be at least partially attributed to the Trump administration's strategy of "maximum" economic and political pressure on the Islamic Republic.

However, this retraction is reversible. The infusions of capital inevitably accompanying greater Chinese commercial activity within Iran will do more than simply stabilize the national economy; they will also allow Iran to sustainably fund a full range of activities throughout the region, from support for the Assad regime in Syria to involvement in Yemen's protracted civil war.

Chinese aid can also be expected to help bolster the Iranian regime's hold on power at home. More than a decade ago, Chinese tech conglomerates played a crucial role in assisting Iran's government in reasserting domestic control in the wake of the 2009 "Green Movement." This activity and assistance has persisted, despite U.S. sanctions. The broader technological footprint envisioned for China in the Islamic Republic as part of the new deal will grant Iran's rulers still greater access to the technologies and surveillance methods that China has used so successfully to control its own population.

A Challenge for Washington

The new Sino-Iranian accord comes amid rapidly rising global tensions between Washington and Beijing. While the Trump administration has long asserted the need for "great power competition" with China, since the beginning of the year this focus on confronting China in economic, strategic, and geopolitical terms has dramatically intensified against the backdrop of the coronavirus pandemic.

Beijing, too, appears to be pivoting toward more direct confrontation. Over the past two years, Chinese oil imports from Iran have declined significantly in response to intensifying U.S. pressure. Last year, for instance, Chinese purchases of Iranian crude shrunk by nearly 53 percent, reflecting a desire on China's part to avoid direct conflict with the Trump administration over Iran. Now, however, Beijing has placed itself squarely in the path of what is arguably the most significant element of U.S. Mideast policy: the Trump administration's "maximum pressure" campaign against the Islamic Republic. By doing so, China has exhibited a newfound willingness to directly thwart U.S. policy and undermine critical U.S. strategic objectives, both in the Middle East and beyond.

Thus, the new Sino-Iranian accord represents a clear challenge to U.S. interests and credibility. Left undisturbed, the expanded economic and strategic bonds between Beijing and Tehran will help stabilize Iran's rickety regime. They will also serve to undermine the Trump administration's efforts to isolate and weaken the country's clerical elite and thereby curb the Islamic Republic's regional adventurism – all of which makes the new strategic pact between the two countries a critical test not only of Washington's China policy but also of the limits of the Trump administration's "maximum pressure" approach to Iran.

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